BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of	
Amendment of Parts 32 and 64 of the Commission's Rules to Account for Transactions Between Carriers and Their Nonregulated Affiliates	CC Docket No. 93-251

TO THE COMMISSION

REPLY COMMENTS OF SOUTHWESTERN BELL TELEPHONE COMPANY

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CC Docket No. 93-251

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Table of Contents

SUMMARY*

As the majority of the commentors note, the proposed changes are unsupported by the record and represent a more burdensome, costly, less accurate and more speculative methodology than the existing rules, which have not been shown to be deficient.

The five commentors favoring the adoption of the rules fail to provide any meaningful argument as to why the Commission should reverse itself and abandon the existing affiliate transaction rules promulgated in the Joint Cost Order Proceeding. The changes proposed in the NPRM should be rejected in their entirety.

The Commission should also reject the language or "notation in the record" proposed by the Texas PUC regarding ICB rates. The Texas PUC suggestion is inconsistent with the rationale underlying the use of a tariffed rate as the first tier of the affiliate transaction rules and would add unnecessary ambiguity and confusion to the rules. If a carrier were to charge an affiliate the higher of fully distributed cost or fair market value instead of the tariffed ICB rate available to the affiliate's competitors, the carrier would be in violation of the Communications Act or applicable state statute regarding nondiscriminatory treatment.

*All abbreviations used herein are referenced within the text.

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Southwestern Bell Telephone Company files this reply to comments filed in response to the Federal Communications Commission's (Commission) Notice of Proposed Rulemaking[1] proposing extensive changes to the existing affiliate transaction rules.

I. THE PROPOSED CHANGES ARE UNSUPPORTED BY THE RECORD AND REALITY.

The proposed changes are a major step in the wrong direction and inconsistent with the public messages being espoused by the Commission Chairman and the Vice President of the United States. As a majority of the commentors note, the proposed changes represent a more burdensome, costly, less accurate and more speculative methodology than the existing rules which have not been shown to be deficient.[2] As the major accounting firm Coopers and

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[1] In the Matter of Amendment of Parts 32 and 64 of the Commission's Rules to Account for Transactions between Carriers and Their Nonregulated Affiliates, CC Docket 93-251, Notice of Proposed Rulemaking (Released October 23, 1993). (NPRM).

[2] AT&T Comments, pp. 14-19; ALLTEL, pp. 2-3; Ameritech Comments, pp. 1, 3-12; Bell Atlantic Comments, pp. 1-4; BellSouth Comments, pp. 4-13; GTE Comments, pp. 2-10; International Communications Association (ICA) Comments, pp. 5-6; NYNEX Comments, pp. 2-13; Southern New England Telephone Company (SNET) Comments,

Lybrand explains:

> **The adoption . . . will add substantial difficulty to the Carrier's affiliate transaction process and complexity and subjectivity to the audit process thereby diminishing the enforcement mechanism that the FCC currently has in place. . . The proposed rules . . . create a complete new layer of work to value services, make it far more difficult for companies to determine whether they are in compliance with rules, add complexity and subjectivity to the audit process and render the company and auditor conclusions subject to continued debate because the market valuation of services adds substantial subjectivity to the rules.**[3]

The proposed changes to the rules and procedures are thus inconsistent with and contradict the "more simplified regulatory scheme" advocated by Reed Hundt, the Commission's new Chairman.[4] They are also inconsistent with and contradict Vice President Gore's proposal to eliminate 50% of internal government regulations over the next three years.[5] The Commission's own Office of Management and Budget (OMB) filing indicates that the proposed changes will add over 320,000 hours of additional work and burden.[6] USTA estimates that Tier I carrier costs will be increased by

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pp. 1-6; Sprint Comments, pp. 2-5; USTA Comments, pp. 2-8, 14-24; U S WEST Comments, pp. 1-5; SWBT Comments, pp. 2-7.

[3]Coopers and Lybrand Comments, p. 4.

[4]"New FCC Chief Signals Change", Communications Week, December 6, 1993, p. 1, at p. 86. See also, SNET Comments, pp. 1-2.

[5]"'Reinvention' Plan Favors 'Electronic Government'," Telecommunications Reports, September 13, 1993, at 25-26; See also, Pacific Bell and Nevada Bell Comments, p. 6.

[6]FCC Public Notice, Public Information Collection Requirement submitted to the OMB (Released November 12, 1993).

approximately $91 million dollars annually by the proposed fair market value estimation alone.[7] Further, AT&T rightfully concludes that the costs for the proposed nut and bolt tracing of transactions would be staggering and that the cost of trueing-up the books on a quarterly basis as proposed in the NPRM will far exceed any value to be gained.[8]

SWBT and various other commentors (including the ICA, which supports the proposed changes), note that the NPRM lacks a legitimate rationale for the proposed changes in the existing affiliate transaction rules.[9] The only justification for such expenditures and unnecessary use of Commission resources is not factual evidence of what has occurred but rather idle speculation and "what-ifs" which were dismissed by the Commission at the time the current rules were adopted.[10] Idle speculation and "what-ifs" simply do not justify the increased expense and burden the changes in the rules will impose on the industry and the Commission,

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[7]USTA Comments, p. 10. This estimate does not include smaller exchange carriers.

[8]AT&T Comments, pp. 17-18.

[9]BellSouth Comments, p. 4; Sprint Comments, pp. 2-3; Ameritech Comments, p. 3; PacTel Comments, pp. 6-7; NYNEX Comments, p. 2; USTA Comments, p. 2; SNET Comments, p. 2; International Communications Association (ICA) Comments, p. 5.

[10]See, Separation of Costs of Regulated Telephone Service From Costs of Nonregulated Activities and Amendment of Part 31, the Uniform System of Accounts for Class A and Class B Telephone Companies to provide for Nonregulated Activities and to Provide For Transactions Between Telephone Companies and Their Affiliates, CC Docket 86-111, 2 FCC Rcd 1298 (1988) (Joint Cost Order); recon. 2 FCC Rcd 6283 (1987) (Joint Cost Recon. Order); Further recon. 3 FCC Rcd 6701 (1988).

especially when a major component of the methodology (i.e., estimated market value/dual basis test) was previously rejected by the Commission as being too speculative, difficult to monitor, and harmful to the economies of scope and scale.[11]

The existing rules were not hastily adopted as some knee-jerk reaction to the perceived need for rules to protect against cross-subsidization. Rather, the rules were debated and promulgated through the lengthy Joint Cost Proceeding, wherein sixty-eight parties filed initial comments and forty-one parties filed reply comments to the Notice of Proposed Rulemaking alone.[12] Twenty-one Petitions for Reconsideration were filed, followed by opposition comments by twenty-one parties and replies by nineteen parties.[13] After the Commission issued its Order on Reconsideration, the industry and the Commission worked through the Cost Allocation Manual (CAM) approval process wherein the rules were further refined as each carrier's CAM was filed and put out for public comment. As the various commentors note, all the effort and work conducted by the Commission and the industry in the Joint Cost Proceeding and the subsequent proceedings has resulted in an affiliate transaction rule methodology and series of safeguards (including audits and the public filing of various reports) which are more than adequate to protect against any perceived threat of

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[11]See, Joint Cost Order, 2 FCC Rcd at 1335; Joint Cost Recon. Order, 2 FCC Rcd at 6297; SWBT Comments, pp. 13-32; See also, fn. 2 supra.

[12]Joint Cost Order, 2 FCC Rcd at 1340-42.

[13]Joint Cost Recon. Order, 2 FCC Rcd at 6307-08.

cross-subsidization.[14] The previous work of the Commission and the industry should not be summarily dismissed, especially when the only rationale is speculation and "what-ifs" which were dismissed when the existing rules were being debated and promulgated in the Joint Cost Proceeding.

Only five of the twenty-two parties filing comments support the NPRM's proposed changes in whole or in part.[15] Those five commentors fail to cite any rationale for the proposed changes in the rules other than repeating the speculation set forth in the NPRM.[16] In fact, even ICA -- which supports the changes -- acknowledges that the NPRM lacks sufficient support for the conclusion that "the current affiliate transaction rules need to be greatly strengthened."[17] ICA "recommends that the Commission provide more details and citations to support its conclusions."[18]

The entire purpose of the NPRM process is to allow all interested parties to comment on the rationale or basis for the change in the existing rules. Failure to express the basis for the change in the NPRM renders the entire NPRM process meaningless. The changes proposed in the NPRM should be rejected in their

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[14]SWBT Comments, pp. 2-7; USTA Comments, pp. 2-8; NYNEX Comments, pp. 3-7; BellSouth Comments, pp. 1-9; See also, fn. 2.

[15]Information Technology Association of America (ITAA); ICA; MCI Telecommunications Corporation (MCI); Tennessee Public Service Commission; Public Utility Commission of Texas (Texas PUC).

[16]See, ITAA Comments, pp. 2-4; ICA Comments, pp. 5-6; MCI Comments, pp. 3-5.

[17]ICA Comments, p. 5.

[18]Id.

entirety.

I. THE COMMISSION SHOULD NOT ADOPT THE TEXAS PUC SUGGESTIONS.

The NPRM proposes to treat affiliate transactions as being provided pursuant to tariff only if the tariff is generally available, on file with a federal or state agency, and in effect.[19] The Texas PUC proposes to add ambiguity to this general rule by stating that the tariffs must be "generally available at a specific dollar-and-cents rate." The Texas PUC does not expand on what it means by a "specific dollar-and-cents rate" but claims that the language would specifically exclude a tariff with an Individual Case Basis (ICB) rate.[20] The Texas PUC suggests that, if the language is not adopted, the Commission should indicate in the record that it "intends for the language in 32.27(b) to exclude a tariff with an ICB notation."[21]

The Texas PUC suggestion that any tariff with an ICB notation be rejected as a tariffed rate is unsupported by the rationale for using a tariffed rate as the first tier of the affiliate transaction rules and represents a case of inappropriate

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[19] NPRM, para. 14.

[20] Texas PUC Comments, p. 3. The use of the term "dollars-and-cents rate" is confusing because all rates are charged in dollars and cents. The listing of a rate as an ICB rate does not mean that the customer is not going to be charged a dollars and cents rate.

[21] Texas PUC Comments p. 3. The Texas PUC includes a definition of ICB from SWBT's Access Service Tariff on file with the Texas PUC. Obviously, the definition of an ICB will vary from jurisdiction to jurisdiction. The Texas PUC Comments do not address how the ambiguous term ICB would be defined for the purpose of its proposed notation "in the record."

stereotyping. The stereotyping occurs because the suggestion erroneously implies that the ICB rates are determined solely by the carrier and the customer and that it is nothing more than an agreed to rate between the two parties. Nothing could be further from reality.

The NPRM acknowledges that a tariffed rate is used as the first tier of the affiliate transaction rule hierarchy because "tariffed rates are subject to federal and state regulation."[22] That includes an ICB rate for a service subject to an appropriate agency's regulatory jurisdiction and offered through the carrier's filed tariffs. Because it is tariffed, the appropriate regulatory agency has approved of the use of the ICB rate and whatever methodology is used to develop the rate. An ICB rate developed pursuant to a generally available state or federal regulatory tariff should not suddenly lose its legitimacy merely because an affiliate is involved. Furthermore, the Texas PUC seems to take the position that an ICB rate is a rate for nonaffiliates but not a rate for affiliates.

The Communications Act, and presumably all states, have a requirement that all tariffed services must be offered on a nondiscriminatory basis.[23] For example, the Communications Act

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[22]NPRM, para. 14.

[23]See, 47 U.S.C. 202(a); See also, e.g., Texas Public Utility Regulatory Act (PURA) Section 45, "No public utility may, as to rates or services, make or grant any unreasonable preference or advantage to any corporation or person within any classification or subject any corporation within any classification to any unreasonable prejudice or disadvantage." (PURA Sec. 45); Mo. Ann. Stat., Sec. 392.200, "No . . . telephone corporation shall make or

provides that it is "unlawful for any common carrier to make any unjust or unreasonable discrimination in charges, practices . . . directly or indirectly, by any means or device, or to make or give any undue advantage to any particular person . . . or to subject any person . . . to any undue prejudice or unreasonable prejudice or disadvantage."[24] The Texas PUC proposal and speculation assumes, without any proof or evidence, that carriers will totally ignore the nondiscrimination provisions and knowingly violate the law. Such an assumption of unlawful activity is not only unsupported in fact but is patently unjust and unfair.

Charging the affiliate the higher of fair market value or fully distributed cost (FDC) instead of a tariffed ICB rate, which by statute must not be unreasonably discriminatory, like the affiliate's competitors, would constitute a violation of the nondiscrimination statutes.[25] The carrier would be discriminating against the affiliate and subjecting the affiliate to "undue and

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give any undue or unreasonable preference or advantage to any person, corporation or locality, or subject any particular person, corporation or locality to any undue or unreasonable prejudice or disadvantage in any respect whatsoever;" (Sec. 392.200(3); Ark. Stat. Ann. Sec. 23-3-114)." As to rates or services, no public utility shall make or grant any unreasonable preference or advantage to any corporation or person or subject any corporation or person to any unreasonable prejudice or disadvantage. (Sec. 23-3-114(a)(1).

[24]47 U.S.C. 202(a).

[25]SWBT assumes that the Texas PUC argument intends the carrier to charge the affiliate the higher of FDC or fair market value.

unreasonable prejudice" and "disadvantage."[26] The purpose of the affiliate transaction rules is to prevent perceived cross-subsidizations not penalize the carrier for selling services to an affiliate. The Texas PUC suggestions should be rejected.[27]

III. THE USE OF THE PREVAILING PRICE TEST SHOULD NOT BE LIMITED BY AN ARBITRARY BRIGHT LINE TEST.

With the usual exception of MCI,[28] the carriers unanimously agree that the imposition of a "bright line test" to limit the use of the well established prevailing price tier of the affiliate transaction rule hierarchy is unnecessary.[29] Even MCI acknowledges, however, that there "is no scientific way to identify

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[26] See, 47 U.S.C. 202. Texas PURA Sec. 45; Mo. Ann. Stat. Sec. 392.200 (3); Ark. Stat. Ann. Sec. 23-3-114(a)(1). It is nonsensical to believe that discrimination in rates based on mere affiliation is just or reasonable. This is especially true when the carrier is required by law to calculate the rate in a nondiscriminatory manner.

[27] See, Texas PUC Comments, p. 3, paras. 6-7.

[28] MCI's continued support of more burdensome regulation on other carriers is consistent with its recent public announcement of competing in the local exchange market in addition to its competing in other markets. MCI recently issued a press release announcing the creation of a new subsidiary that "is expected to invest $2 billion in fiber rings and local switching infrastructure in major U.S. metropolitan markets . . . to begin providing alternative local telecommunications facilities." The press release further notes that the subsidiary owns properties and rights-of-way in several hundred cities and is currently the fourth largest competitor to the Bell Operating Companies in providing local access to long distance service.

[29] Ameritech Comments, pp. 19-21; BellSouth Comments pp. 20-22; NYNEX Comments, pp. 24-26; SNET Comments, pp. 7-8; US West Comments, pp. 17-19; GTE Comments, pp. 11-13; USTA Comments, pp. 18-20; AT&T Comments, p. 18; Sprint Comments, pp. 6-10; SWBT Comments, pp. 7-13.

the actual percentage of sales at which the necessary degree of assurance of veracity is reached, so any level selected necessarily will be somewhat arbitrary."[30] Moreover, as the majority of commentors note, the use of a percentage "bright line test" is not only arbitrary but unnecessary because the percentage of output test has nothing to do with the establishment of a market price.[31] It is the willingness of nonaffiliated third parties to pay that price which establishes a prevailing price, not what arbitrary percentage is sold to affiliates.

MCI claims that "carriers have virtually total control over their claimed levels of prevailing company prices."[32] MCI's comments indicate a basic misunderstanding of the existing prevailing price rules. As SWBT notes in its comments, in order to establish a prevailing price, the Commission rules require that there be a substantial number of actual sales to nonaffiliated third parties at that price.[33] Failure to follow such rules and the rules for calculating FDC if prevailing price is not established, leaves a carrier subject to enforcement action by the Commission including possible forfeitures, in addition to the stigma of having been found to have violated the Commission's rules. Given the Commission's rules and the consequences

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[30]MCI Comments, p. 5.

[31]SWBT Comments, pp. 11-13; BellSouth Comments, pp. 20-23; SNET Comments, pp. 7-8; GTE Comments, pp. 11-13; AT&T Comments, p. 18.

[32]MCI Comments, p. 4.

[33]SWBT Comments, p. 10.

associated with violating such rules, MCI's statement that there "are no firm guidelines that ensure that the price recorded on the books of either entity engaged in a transaction has any relation to either the professed market price or to its underlying cost"[34] is simply ludicrous.

IV. THE USTA GENERIC RATE BASE CALCULATION SHOULD BE ADOPTED.

SWBT concurs with the majority of the commentors that the USTA Generic Rate Base calculation continues to be the most appropriate method for developing the FDC element.[35] SWBT also agrees with NYNEX that the authorized interstate rate of return, currently established at 11.25%, is a simple way to establish the return element, avoid confusion and controversy and minimize the need for true-up activity.[36]

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[34]MCI Comments, p. 4.

[35]Ameritech Comments, p. 25; CBT Comments, p. 9; ALLTEL Comments, p. 3; GTE Comments, p. 1; USTA Comments, pp. 24-25; NYNEX Comments, pp. 31-32; Sprint Comments, p. 24.

[36]See, NYNEX Comments, p. 33.

V. CONCLUSION

For the reasons stated herein and in SWBT's initial comments, the proposals contained in the NPRM should be summarily rejected in their entirety.

Respectfully submitted,

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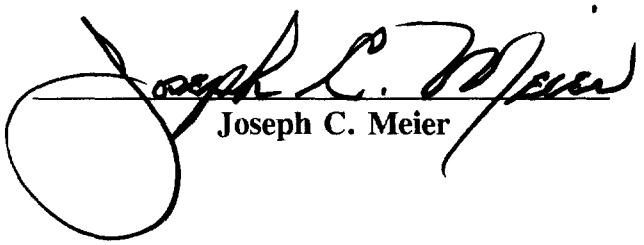
CERTIFICATE OF SERVICE

I, Joseph Meier, hereby certify that the foregoing "Reply Comments Of Southwestern Bell Telephone Company", in CC Docket No. 93-251, has been served this10th day of January, 1994, to the Parties of Record.



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